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***December 30, 2002***

***To the Citizens of the Commonwealth of Massachusetts,  
Governor Jane Swift, and Honorable Members of the General  
Court***

I am pleased to transmit to you the Commonwealth's fiscal 2002 Comprehensive Annual Financial Report (CAFR) in the new format prescribed under Government Accounting Standards Board (GASB) Statements 34, 35, 37 and 38. This report is the culmination of a three-year process that involved many departments and authorities of the Commonwealth and countless hours of analysis, preparation and audit.

The report is the primary means of reporting the Commonwealth's financial activities. The objective of this new model is to provide a clearer picture of our government as a single, unified entity, while retaining certain traditional financial information previously provided.

This document presents the Commonwealth's financial information on three bases of accounting, each serving a different purpose. The back of the book includes as "required supplementary information" budgetary basis statements, which are prepared in accordance with the Commonwealth's budgetary process. In the Commonwealth this is referred to as statutory basis. More detailed information on the statutory basis of accounting and the results on that basis from fiscal 2002 are found in the Statutory Basis Financial Report (SBFR) separately issued this past October. The SBFR report documents compliance with the legislatively adopted budget. Each state maintains different rules for this basis and therefore these statements should not be used for comparison across states.

The fund perspective statements on pages 37 to 49 present the governmental operation on the same basis (modified accrual basis of accounting) as previous CAFR's with one exception. The account groups for long-term debt and fixed assets have been deleted. In addition, there is a perspective difference. Certain funds that are shown as fiduciary under this perspective are not portrayed under GASB34, or are reclassified. This basis is designed to measure inter - period equity, the extent to which current resources (available within the next year) fully fund all current services provided by the government. Long - term liabilities are excluded with the implicit assumption that future tax revenues will fund them. This fund perspective continues to provide results similar to the statutory basis financial statements published in October.

In addition to this "fund perspective," the new CAFR presents an "entity wide" perspective. This perspective combines all governmental and business activities in a statement of net assets and a statement of activities, presenting all functions on a full accrual basis of accounting. All fixed assets, including road and bridge infrastructure, are added to the statements as are long - term liabilities such as outstanding debt.

The balance sheet has been reorganized into a “net assets format.” This format classifies assets and liabilities as short and long-term and then subtracts those liabilities from assets to arrive at net assets similar to a private company. Second, the statement of net assets includes capital assets not previously found on the Commonwealth’s balance sheet, including the historical cost of infrastructure including roads, bridges, tunnels and dams owned by the Commonwealth, net of accumulated depreciation. It also includes the long – term debt and commitments of long - term assistance to municipalities and authorities, previously not in the calculation of fund balance.

The Commonwealth’s statement of revenues, expenditures and changes in fund balances has been completely reorganized to a new statement of activities. The expenses of the Commonwealth, organized by activity, are netted against fees, fines, grant revenues and assessments generated to fund each activity in an attempt to derive the net cost to the taxpayer of each activity. The reader of the financial statements can now discern the net cost of a particular function of government funded by taxation and other general revenues by a review of this statement.

To understand the difference between the Commonwealth’s budgetary fund balance and the GAAP basis fund perspective balance, as depicted in the fund financial statements and the Commonwealth’s governmental financial position under this new presentation, a series of accruals and adjustments must be analyzed as follows:

**Governmental Funds - Statutory to GAAP - Fund Perspective and to  
Governmental Net Assets**  
(Amounts in millions)

<b>Governmental Fund Balance - Statutory Basis, June 30, 2002.....</b>	<b>\$ 2,274.4</b>
Plus: Expendable Trust and Similar Fund Statutory Balances that are	
considered Governmental Funds under GASB 34.....	229.9
Liability Management Fund Net Assets.....	1.7
Owner Controlled Insurance Program Net Assets.....	239.9
Debt Service Fund Net Assets.....	<u>236.5</u>
<b>Adjusted Statutory Governmental Fund Balance .....</b>	<b>2,982.4</b>
Accruals, net of allowances and deferrals for {Increases / (decreases)}:	
Taxes.....	\$ 646.5
Medicaid.....	(393.1)
Compensated absences.....	(246.1)
MBTA.....	(23.7)
Massachusetts Water Pollution Abatement Trust.....	(33.8)
Massachusetts Turnpike Authority.....	(16.1)
Regional transit authorities .....	(72.5)
Other nonmajor component unit accruals .....	(4.6)
Uncompensated care liability .....	(110.3)
Claims, judgements and other risks.....	(76.1)
Workers' compensation and group insurance .....	(85.3)
Other accruals .....	<u>(99.4)</u>
Net increase / (decrease) to governmental fund balances.....	<u>(514.5)</u>
<b>Governmental fund balance (fund perspective) .....</b>	<b>\$ 2,467.9</b>
Plus: Fixed asset including infrastructure.....	25,641.2
Less: Accumulated depreciation.....	(6,414.3)
Plus: Deferred revenue.....	317.1
Less: Long term liabilities .....	<u>(29,427.4)</u>
<b>Total governmental net assets (entity wide perspective).....</b>	<b><u>\$ (7,415.5)</u></b>

This CAFR is presented in three sections: **Introductory**, **Financial** and **Statistical**. This **Introductory Section** contains an overview of the Commonwealth's economic performance, a review of current initiatives and summary financial data. This section contains information that existed as of June 30, 2002. The **Financial Section** contains a Management's Discussion and Analysis (MD&A) section. Generally Accepted Accounting Principles (GAAP) require that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of MD&A. This letter of transmittal is designed to complement MD&A where the financial analysis is now presented. The Commonwealth's MD&A can be found immediately following the independent auditor's report from Deloitte and Touche, LLP. The **Statistical Section** contains selected financial and demographic information. It also contains background information on the Commonwealth.

## **PROFILE OF THE COMMONWEALTH**

### **REPORTING ENTITY**

The financial statements incorporate 156 departments. These departments include the various agencies, boards, and commissions, the 25 institutions of higher education, the judicial and legislative branches of government, and constitutional offices.

The departments record their daily financial operations in the state accounting system called the Massachusetts Management Accounting and Reporting System (MMARS) operated by the Office of the Comptroller.

In addition, the financial statements include 28 independent public authorities and the State Employees' and Teachers' Retirement Systems. These component units meet the criteria for inclusion in the reporting entity in accordance with GAAP, which are further described in Note 1 to the financial statements.

### **INDEPENDENT AUDIT**

The Commonwealth's independent auditors, Deloitte and Touche, LLP, together with subcontractors Daniel Dennis & Company, Margaret Carr, CPA and Susan Perna-Damon, CPA with assistance by the Office of the State Auditor (OSA) have performed an independent audit of the Commonwealth for the fiscal year ended June 30, 2002. OSA also plays a large role in the simultaneous audit of the Schedule of Federal Financial Assistance of the Commonwealth, as prescribed in the Federal Office of Management and Budget's Circular A-133.

We express our gratitude to the staff of the respective firms and the Office of the State Auditor for their professionalism, advice and counsel. The independent auditor's report is presented in the Financial Section.

The OSA is statutorily mandated to perform audits of the accounts, programs, activities and functions of all departments, offices,

commissions, institutions and activities of the Commonwealth. OSA provides its knowledge, expertise, experience and resources as a participant in the single audit of the Commonwealth, which encompasses all of the Commonwealth's financial operations. A more complete discussion of this work can be found in the State Auditor's semi-annual report available on their web site: <http://www.mass.gov/sao>.

The Office of the Comptroller prepares these statements and assumes full responsibility for the completeness and reliability of the information presented in this report. To provide a reasonable basis for making these representations, the Office of the Comptroller, working in conjunction with the State Auditor, has established a comprehensive internal control framework that is designed to protect the Commonwealth's assets from loss, theft, or misuse and to compile sufficient reliable information for the preparation of the Commonwealth's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the Commonwealth's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement.

## **GOVERNMENT FINANCE OFFICER'S ASSOCIATION AWARD**

In fiscal year 2002, the Government Finance Officer's Association awarded a Certificate of Achievement for Excellence in Financial Reporting to the Commonwealth for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2001. The Certificate of Achievement is a prestigious national award, recognizing conformance with the highest standards for preparation of state and local government financial reports. This is the twelfth consecutive year that the Commonwealth has received this award.

## **RECOMMENDATIONS, CONCLUSIONS AND OTHER ACCOMPLISHMENTS**

The Commonwealth has many accomplishments in fiscal 2002 of which it can be proud.

The Office of the Comptroller has undertaken a major effort to build a more collaborative working relationship among members of this office and Chief Fiscal Officers (CFOs) of the Commonwealth in a program we call "PARTNERS in Financial Management" The second CFO conference brought together CFOs from across the Commonwealth for two days of meetings. PARTNERS stands for people, accountability, responsibility, trust, negotiation, efficiency, risk assessment and mitigation, and solutions. We have enhanced the mantra that all systems, big and small, depend on people who are integral to those systems. This recognizes that fiscal officers of the Commonwealth are all accountable for their actions, ensuring the uncompromising integrity of the financial statements of the Commonwealth. We must maintain this standard to maintain the public trust. The Office of the Comptroller continued to increase delegation this year to individual departments due to the level of trust that we have with them, based on prior results. We

must continually strive to balance accountability with efficiency, especially in order to continually serve the citizens of the Commonwealth, our customers. This balancing also targets controls to result in effective risk mitigation. Finally, we strive to find solutions to many of the Commonwealth's problems in conjunction with the rest of the CFOs, so that full input is heard.

Last year, the Commonwealth started the process of consolidating its web sites to better serve the citizens of the Commonwealth. With service to our citizens as key, the Commonwealth's new web portal "Mass.Gov" promises to bring government closer to the people. Mass.Gov is customer-focused. It provides services according to the needs of citizens and businesses, not according to government structure. Citizens are able to quickly find the information and services they need without having to navigate the bureaucracy of government. Mass.Gov provides comprehensive, integrated, and seamless services that our citizens will be able to bring into their homes or businesses at their convenience, twenty-four hours a day, seven days a week. The Office of the Comptroller contributed to joint projects with ITD to build internet based shared services for use by all internet based applications. In addition we continued to roll out new technology with real benefits to state departments and taxpayers. This year we released an internet based front end to the Billing and Accounts Receivable System allowing institutions of higher education to provide information regarding non performing receivables to the Comptroller for potential intercept against Commonwealth payments or tax refunds. This technology was developed so that any government entity authorized in statute could take advantage of this tool. In addition we piloted new financial software simplifying the vendor registration process, reducing administrative workloads in departments and reducing the time from contract registration to completed vendor registration.

In May of 2002, the Legislature enacted Information Technology Bond III, authorizing \$300 million for the Commonwealth to upgrade its technology infrastructure. Included in this legislation is funding for the Commonwealth to upgrade the statewide financial system from the 1980's, MMARS to a state of the art internet-based financial system. Last month, the Office of the Comptroller and the Information Technology Division entered into a joint project with American Management Systems, (AMS), of Fairfax, Virginia, to upgrade this key financial system. The new system is slated to be completed in time for the opening of FY05. This project will focus on changing business practices in order to minimize customization to this product. This strategy will insure the Commonwealth can upgrade to current releases in the future at a reasonable cost. The goal is to keep current with technology in the future and at the same time control the total cost of system ownership. Benefits will accrue directly to the users of the financial system. In addition, this updated technology will allow for the future integration of Commonwealth internet-based applications into "back office" financial systems. The Comptroller, the Information Technology Division and AMS have assigned a highly motivated, highly dedicated team to this project to insure its success.

I again would like to express my thanks to the many dedicated people within the Office of the State Comptroller. We have had another successful year within the office. I must express special thanks to those

in the Commonwealth who worked tirelessly to implement the new financial statement. Individuals throughout state government valued and depreciated infrastructure. Institutions of higher education and the Commonwealth public authorities needed to work in concert with their auditors and my office to adopt and implement new accounting policies and procedures. This additional work came at a time when administrative resources were being reduced. While many governments sought additional resources for this task, the Commonwealth redeployed existing resources to implement this standard at no additional cost. Special thanks goes to Eric Berman who led this effort on behalf of the Commonwealth and is now looked to nationally as one of government's leading experts on this new standard. To Eric and the Financial Reporting and Analysis Bureau – I thank you. Our office has undertaken many tasks this year. We are embarking on the redesign of the state accounting system, MMARS. This will be a significant effort but will provide enduring benefits to the Commonwealth. I am proud to have all the employees of the Comptroller's Office on my team to help tackle these and other difficult issues in the future.

Respectfully submitted,

Martin J. Benison  
Comptroller of the Commonwealth